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ABSTRACT

Creating opportunities for high-growth entrepreneurs is becoming increasingly important in rural America. Rural policymakers, who once focused on recruiting manufacturers that export low-value products, have realized that entrepreneurs can generate new economic value for their communities. Entrepreneurs add jobs, raise incomes, create wealth, improve the quality of community life, and help rural communities operate in the global economy. Each year, high-growth entrepreneurs create the bulk of new jobs in the United States. Still, rural America is creating relatively few high-growth entrepreneurs. To overcome the challenges of being small and remote, rural communities must help entrepreneurs tap venture capital markets to finance growth. They must help entrepreneurs gain access to the information and technology needed to spur growth. And they must help entrepreneurs acquire the technical and managerial skills to cultivate that growth. Rural policymakers are responding to these challenges by making entrepreneurship the cornerstone of many economic development strategies. Their strategies aim to build the skills of individual entrepreneurs, strengthen community resources for entrepreneurs, and create support networks. Universities and community colleges are offering entrepreneurship courses, and extension services provide programs to improve entrepreneurs' technical and Internet skills. Rural support networks are emerging in various forms, including networks of business incubators, angel investors, and technical assistance organizations. (TD)

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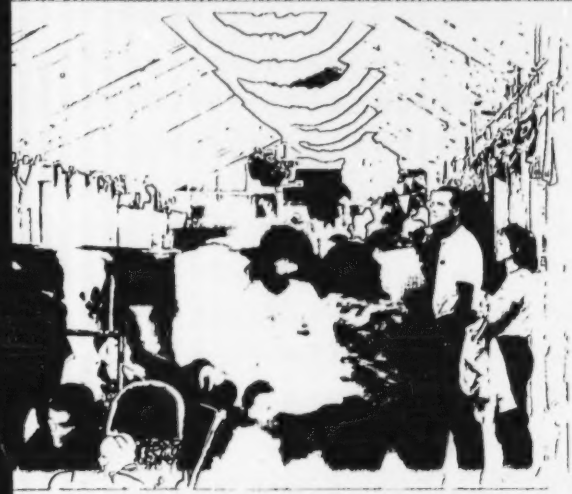
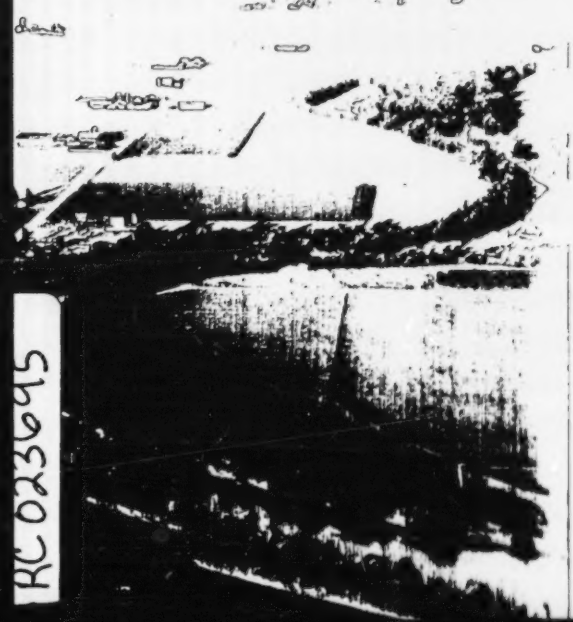
The Main Street Economist
Commentary on the rural economy





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Are High-Growth Entrepreneurs Building the Rural Economy?

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New technologies, products, and services are brought to market every year by small entrepreneurs. The heart valve, safety razor, and soft contact lens are just a few examples. One common thread ties all successful entrepreneurs together—innovation. Innovation brings something new or unusual to the marketplace, and in the process sharpens competitiveness and creates wealth. New firms, new products, and new ways of doing business all add value to a community and improve the quality of life for its citizens.

Recognizing that innovation and entrepreneurs are a wellspring of opportunity, many rural policymakers are rethinking their strategies for spurring economic development. Instead of trying to lure existing manufacturing plants from other places, many communities are shifting their focus to growing their own entrepreneurial firms. Many new firms fail, of course. But those that succeed can add new jobs, lift incomes, generate new wealth, and help connect the community to the larger, global economy.

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Entrepreneurial firms have a proven track record. The Small Business Administration consistently reports that small and medium-sized businesses account for about two-thirds of all new jobs in the U.S. economy each year. And, the earnings of successful self-employed entrepreneurs are almost one-third higher than those of wage and salaried workers.

It's important to recognize, however, that the benefits of entrepreneurs can vary dramatically, depending on the entrepreneur's desire to build a high-growth business—the kind of businesses that rural areas often lack. This article examines entrepreneurial activity in rural America and discusses some of the ways rural policymakers are beginning to encourage high-growth entrepreneurs in their communities.

High-growth vs. lifestyle entrepreneurs

The benefits of entrepreneurs often depend on the entrepreneur's goal for starting a firm. According to the Kauffman Center for Entrepreneurial Leadership, *lifestyle entrepreneurs* generally start new firms to provide a family income or support a desired lifestyle. These entrepreneurs typically seek independence and control over their own schedule. Because of their lifestyle focus, the benefits of these entrepreneurs relate primarily to the quality of life in local communities, providing many of the services needed by local residents. And, perhaps most important, they add personality to Main Street economies—the charm that attracts many people to shop and live in rural communities.

High-growth entrepreneurs, in contrast, typically set out to develop larger, highly visible, and more valuable firms. These entrepreneurs commonly focus on obtaining the resources necessary to fuel growth. Many seek to take the business public after obtaining some degree of success. The presence of a significant innovation that has dramatically changed the competitive climate of the market characterizes many high-growth entrepreneurial firms.

In the minds of many community leaders, high-growth entrepreneurs provide the biggest economic benefit to their communities. In addition to creating more jobs, more income, more wealth, and a larger tax base for their communities, high-growth entrepreneurial companies often re-invest in their communities. Many have become the cornerstones of their rural communities. For example, Pella Corporation in Pella, Iowa, has grown into one of the world's largest window manufacturers and has been identified as one of the 100 best companies to work for by *Fortune* magazine.

High-growth entrepreneurs in rural America

A simple way to determine how many entrepreneurs there are in rural America is to look at the number of self-employed workers. That number slowed in the 1980s, but rebounded in the 1990s, outpacing the growth of self-employed workers in metro areas (Chart 1). Self-employed workers received higher personal income levels than other rural workers. In 2001, the average self-employed rural worker reported personal income of roughly $33,000, compared with $27,000 and $30,000 for rural private and government workers.

Yet while rural America is growing entrepreneurs, a closer look at the data reveals relatively few high-growth entrepreneurs. Simply put, rural entrepreneurs tend to build smaller firms and generate lower incomes. In 2001, according to the Current Population Survey, 85 percent of the rural self-employed operated firms with less than ten employees. Only 5.5 percent of the rural self-employed worked in firms with more than 100 employees. That figure was only about half that of the self-employed in metro areas. And, in 2001, the rural self-employed earned about 42 percent less than the metro self-employed.

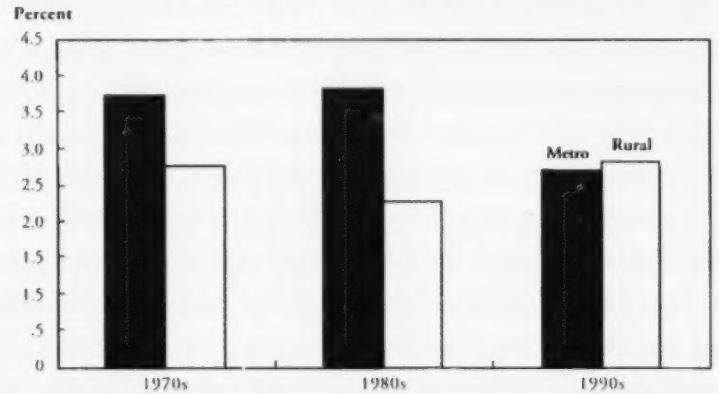
The lack of high-growth entrepreneurs in rural areas is reflected in the differences between incorporated and unincorporated self-employed. Incorporated self-employed tend to have larger incomes and larger firms, indicators of high-growth firms. In 2001, the personal income level for incorporated rural self-employed was almost double the income of rural unincorporated self-employed. But in 2001, incorporated self-employed accounted for just one-fourth of all rural self-employed, compared with one-third in metro areas.

Challenges to entrepreneurship

Given that new entrepreneurs are emerging in rural areas, why are rural communities having such a difficult time generating high-growth entrepreneurs? First, it appears that small communities and their remoteness severely limit access to the

Chart 1

Rural and Metro Self-Employment Growth



Source: Dept. of Commerce

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resources they need to create high-growth businesses. Entrepreneurs in rural areas find it harder to access venture capital. Accessing technology can also be more difficult. Finally, rural entrepreneurs often lack the technical or managerial know-how necessary to create high-growth businesses.

Smallness and remoteness of rural areas make it difficult to develop economies of scale and critical mass. The results are higher prices for goods and lower demand for services. The lack of transportation infrastructure, such as airports or interstates, makes it difficult to transport goods and link to outside markets. These reduced linkages also limit the knowledge and technology transfer between remote rural areas and their economic partners.

Accessing venture or equity capital may be the most important hurdle hindering rural entrepreneurship. In many rural places, equity markets either do not exist or are unorganized at best. The lack of information and high transaction costs limits venture capital access for rural entrepreneurs. As a result, from 1995 to 1998, rural entrepreneurial firms acquired a disproportionately small share of U.S. equity financing.[1]

Accessing technology is still a major challenge, even though technological advances such as the Internet are helping some rural areas to overcome this limitation. Internet access is commonly identified as a key part of the equation supporting rural economic development. Rural areas have Internet access, but they usually lack high-speed broadband access, which is vital to e-commerce development. As a result, compared to their metro peers, fewer rural self-employed report using the Internet at work in the 2001 Current Population Survey.

Lower skill levels of rural entrepreneurs can also limit the growth of high-growth entrepreneurs. More advanced education can give entrepreneurs the technical or managerial know-how they need to become high-growth entrepreneurs. Rural incorporated self-employed, who operate larger firms and receive higher incomes, typically have higher education levels than their unincorporated peers. But rural entrepreneurs on average tend to have less education than their metro counterparts. According to the Current Population Survey, less than one-third of rural self-employed have earned a degree, compared to almost half of metro self-employed.

Despite all the challenges, high-growth entrepreneurs sometimes emerge in rural areas. The rural labor market area surrounding Farmington, New Mexico, generated the third-highest share of high-growth entrepreneurs in the United States in the first half of the 1990s. This region was highlighted in a case study at the Center's 2002 annual conference. The case study made it clear that rural communities can overcome the challenges facing rural economic development by partnering with other rural communities in the region. By working together, these communities were able to build economies of scale, access technology and other resources, and overcome political boundaries to generate entrepreneurial and economic growth.

Entrepreneurship in rural development policy

In many respects, by making entrepreneurship a cornerstone of economic development, rural policymakers are forging a new policy frontier. However, the impacts of these activities are largely unknown. Going forward, the impacts must be monitored to ensure that the benefits outweigh the costs.

Policymakers across the United States have initiated three types of policies for encouraging entrepreneurship. Some strategies aim to improve the skills of individual entrepreneurs. Others seek to strengthen community resources for entrepreneurs. And others create networks to help entrepreneurs capture the resources they need. While not all of these policies were designed specifically for rural areas, they address the challenges that rural areas typically face in developing high-growth entrepreneurs.

Recognizing that business success is largely determined by the entrepreneur, many entrepreneur development programs focus on improving the *skills of individuals.* Many programs emerge from partnerships between government and nonprofit organizations. These programs often aim to develop the technical and managerial know-how of individual entrepreneurs to give small business owners and aspiring entrepreneurs the tools they need to become high-growth entrepreneurs.

Universities and community colleges are becoming more involved in improving the skills of entrepreneurs. Many colleges are designing complete curriculums for entrepreneurship training. According to the Harvard Business School, the number of business schools offering entrepreneurship courses rose from six in 1967 to 370 in 1993. In 1997, Harvard Business School opened an outpost in Silicon Valley to support research on entrepreneurship.

At land grant universities, extension services are working to build the technical skills of entrepreneurs. For example, the University of Minnesota extension service has developed the Access Minnesota Main Street program to improve the Internet and e-commerce skills of small and medium-sized businesses in Minnesota. This program has had some success and is being used as a model by the extension services at the University of Nebraska-Lincoln and Penn State University.

While success is determined by the entrepreneur, the opportunity for success must be fostered by the *community environment.* The availability of resources in a community, especially venture capital, is a key to developing high-growth entrepreneurs. In rural areas, social support also fosters growth in entrepreneurial activity. As a result, the focus of many policies is providing venture capital and building an entrepreneurial culture.

Angel investors are quickly becoming a common way to provide venture capital. Angel investors are wealthy individuals willing to provide start-up money for entrepreneurs. They typically provide smaller amounts of venture capital to entrepreneurs than venture capitalists, but the seed money is often an important bridge to other sources of capital. Most angels invest locally within a day's drive of their residence. While angels

remain concentrated in the Silicon Valley and New England, they have been emerging in other parts of the country. For example, in Minnesota the Lakes Venture Group is a group of angels who provide equity capital in addition to management expertise for start-up or early development companies in rural parts of the state.

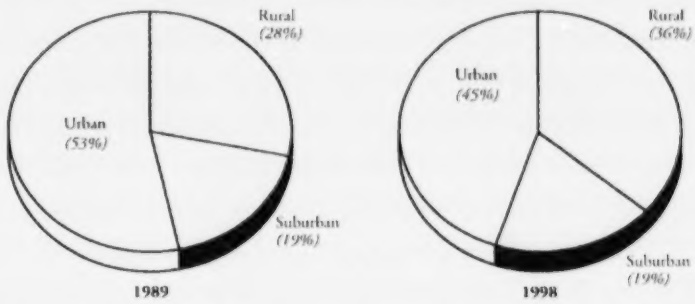
Entrepreneurship programs are trying to overcome the cultural attitudes in rural areas that limit the appreciation of entrepreneurship as an economic development strategy. One way in which attitudes change is through the increased recognition of entrepreneurs. Several states now have small business or entrepreneur-of-the-year awards that highlight the importance of entrepreneurial activity in local economies. Many universities, centers for entrepreneurship, and state governments sponsor business plan competitions that encourage entrepreneurial development. The Center for Rural Entrepreneurship has also initiated a monthly series of stories highlighting entrepreneurial rural communities and individuals. All of these initiatives recognize the importance of entrepreneurship in rural communities.

The secret to developing an entrepreneurial community often lies in the effectiveness of *support networks*. Networks are informal or formal groups of peers or organizations that link entrepreneurs with the social, business, and strategic resources they need to grow. Networks can provide links to new sources of capital, employees, partnerships, and business services. Many seek to provide a support group of peers to generate an entrepreneurial environment. Rural networks are emerging in many forms—as incubator networks, angel investor networks, and other technical assistance network organizations.

Incubator networks are quickly emerging as one of the most common programs to develop entrepreneurs. An incubator is an organization that provides business, management, and marketing resources to start-up firms, along with rental space, shared office services, technology support, and financing assistance. Most incubators are sponsored by government, nonprofit organizations, or academic institutions. By housing multiple startups in a single location, networks emerge as entrepreneurs interact with one another, obtain resources, and grow in an entrepreneurial climate. The goal is to help firms become financially viable and graduate into a freestanding business. According to the NBIA, the number of business incubators jumped from 12 in 1980 to over 900 in 2002. In 1998, 36 percent of the incubators affiliated with the NBIA were located in rural areas, up from 28 percent in 1989 (Chart 2). Almost 90 percent of NBIA incubator graduates were still in business in 2002, with 84 percent staying in their local communities. The National Business Incubator *Association* (NBIA) indicates that each new job created in a publicly supported incubator costs about $1,000, far less than many other job creation strategies.

Chart 2

Location of U.S. Business Incubators



Source: National Business Incubator Association

Conclusion

Creating opportunities for high-growth entrepreneurs is becoming increasingly important in rural America. Rural policymakers, who once followed traditional strategies of recruiting manufacturers that export low-value products, have realized that entrepreneurs can generate new economic value for their communities. Entrepreneurs add jobs, raise incomes, create wealth, improve the quality of life of citizens, and help rural communities operate in the global economy. Each year, high-growth entrepreneurs create the bulk of new jobs in the United States.

Still, rural America is creating relatively few high-growth entrepreneurs. To overcome the challenges of being small and remote, rural communities must help entrepreneurs tap venture capital markets to finance growth. They must help entrepreneurs gain access to the knowledge and innovation outside rural areas needed to spur growth. And they must help entrepreneurs acquire the technical and managerial know-how to cultivate that growth. These are just a few of the challenges limiting the emergence of high-growth entrepreneurs.

Rural policymakers are responding to these challenges by making entrepreneurship the cornerstone of many economic development strategies. Their strategies aim to build the skills of entrepreneurs, develop community resources, and create support networks. As policymakers stretch the frontier of entrepreneurial development, the impacts of these programs will need to be assessed to identify the costs and benefits of supporting high-growth entrepreneurs in rural America.

Edited by Bob Reagan

[1] *Brophy, David J. and Wassim Mourtada. 1999. "Equity Finance and the Economic Transition of Rural America: A New Framework for Private-Sector Initiatives and Positive Economic Public Policy," published in* ***Equity for Rural America: From Wall Street to Main Street****. Federal Reserve Bank of Kansas City. pp. 107-64.*

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